Supreme Court, U.S.
FILED
06-962 JAN 11 2007
OFFICE OF THE CLERK

No. 06-___

In the Supreme Court of the United States

XEROX CORPORATION RETIREMENT INCOME GUARANTEE PLAN, ET AL., PETITIONERS,

v.

WALDAMAR MILLER, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

MICHAEL D. RYAN
XEROX CORPORATION
800 Long Ridge Road
Stamford, CT 06904
(203) 968-3715

RICHARD C. SHEA
DAVID H. REMES
Counsel of Record
THOMAS L. CUBBAGE III
ROBERT S. NEWMAN
MICHAEL E. PAULHUS
COVINGTON & BURLING LLP
1201 Pennsylvania Ave., N.W.
Washington, D.C. 20004-2401
(202) 662-6000

Attorneys for Petitioners

QUESTION PRESENTED

To ensure that an employee receives a minimum level of retirement income, many pension plans coordinate the benefits they provide at retirement with benefits available to the employee from other sources. Coordination typically is accomplished by offsetting the employee's pension benefit by the benefits from the other sources, including benefits the employee receives from the other sources before retirement. The question presented is:

Whether ERISA permits a pension plan, when calculating an employee's accrued pension benefit at retirement, to apply an offset for the benefits the employee receives before retirement from other sources by valuing those benefits in the same way as benefits due at retirement, thus ensuring that employees who receive distributions before retirement from other sources are treated no better than employees who do not receive such distributions.

The Second Circuit has said yes, and the Ninth Circuit has said no, in two cases involving the same nationwide pension plan.

PARTIES TO THE PROCEEDING

The Xerox Corporation Retirement Income Guarantee Plan; Xerox Corporation; and Lawrence M. Becker, as incumbent Plan Administrator of the Xerox Corporation Retirement Income Guarantee Plan, are the petitioners in this Court and were the appellees in the court of appeals.†

Waldamar Miller; Thomas H. Sudduth, Jr.; and J. Denton Allen are the respondents in this Court and were the appellants in the court of appeals.

RULE 29.6 STATEMENT

Xerox Corporation has no corporate parent. No publicly held company owns 10 percent or more of Xerox Corporation's stock.

---

† Patricia Nazemetz, former Plan Administrator of the Xerox Corporation Retirement Income Guarantee Plan, appeared as a defendant and appellee in the proceedings in the district court and court of appeals.

TABLE OF CONTENTS

OPINIONS BELOW .....

STATEMENT .....

REASONS FOR GRANTING THE WRIT.....

CONCLUSION .....

TABLE OF AUTHORITIES

Page

Cases

Alessi v. *Raybestos-Manhattan, Inc.*, 451 U.S. 504 (1981) ..... *passim*

Bonovich v. *Knights of Columbus*, 146 F.3d 57 (2d Cir. 1998) 14

Brengettsy v. *LTV Steel (Republic) Hourly Pension Plan*, 241 F.3d 609 (7th Cir. 2001) 14-15

Frommert v. *Conkright*, 328 F. Supp. 2d 420 (W.D.N.Y. 2004), *aff'd in part, rev'd in part*, 433 F.3d 254 (2d Cir. 2006) 9-10

Frommert v. *Conkright*, 433 F.3d 254 (2d Cir. 2006) 2, 8-10

Hammond v. *Xerox Corp. Ret. Income Guar. Plan*, No. CV 2:97-8349, 1999 WL 33915859 (C.D. Cal. Apr. 8, 1999), *aff'd*, 225 F.3d 662 (9th Cir. 2000) (mem.) 9

Hammond v. *Xerox Corp. Ret. Income Guar. Plan*, 225 F.3d 662 (9th Cir. 2000) (mem.) 7

Lunn v. *Montgomery Ward & Co.*, 166 F.3d 880 (7th Cir. 1999) 4

Patterson v. *Shumate*, 504 U.S. 753 (1992) 8, 11

PPG Indus. Pension Plan A v. *Crews*, 902 F.2d 1148 (4th Cir. 1990) 14

Vintilla v. *U.S. Steel Corp. Plan for Employee Pension Benefits*, 606 F. Supp. 640 (W.D. Pa. 1985), *aff'd mem.*, 782 F.2d 1033 (3d Cir. 1986) (table) 14-15

Williams v. *Caterpillar, Inc.*, 944 F.2d 658 (9th Cir. 1991) 2

Statutes, Regulations, and Administrative Materials

26 U.S.C. § 415 13
28 U.S.C. § 1254 1
29 U.S.C. § 1002 ..... 1, 3, 12
29 U.S.C. § 1053 ..... 1, 6, 12
29 U.S.C. § 1054 ..... 1, 12
29 U.S.C. § 1104 10
29 U.S.C. § 1132 ..... 6, 10

26 C.F.R. § 1.401(a)(4)-3 3
26 C.F.R. § 1.411(a)-7 13

Revenue Ruling 76-259, 1976-2 C.B. 111 ..... *passim*

Proposed Treasury Regulation § 1.415(b)-2, 70 Fed. Reg. 31,213 (May 31, 2005) 3, 13

OPINIONS BELOW

The amended opinion of the court of appeals (App. 1a) is reported at 464 F.3d 871 (9th Cir. 2006). The original opinion of the court of appeals (App. 13a) is reported at 447 F.3d 728 (9th Cir. 2006). The district court's opinion (App. 25a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on May 8, 2006. A petition for rehearing was denied on September 16, 2006. (App. 40a.) The court of appeals' amended judgment was entered on September 13, 2006. On December 4, 2006, Justice Kennedy extended the time within which to file a petition for a writ of certiorari to and including January 11, 2007. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Sections 3(19), 3(22), 3(23), 3(34), 3(35), 203, and 204 of the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §§ 1002(19), 1002(22), 1002(23), 1002(24), 1002(34), 1002(35), 1053, and 1054, are reproduced in the separate appendix to this petition.

STATEMENT

The petition should be granted to resolve a circuit conflict on an important question of ERISA law affecting pension plans nationwide: Does ERISA require an offset for a prior distribution of retirement benefits to be calculated using interest and other assumptions in effect at the time the prior distribution was made to the exclusion of all other methods? Offsets for prior distributions permeate the pension system, and most pension plans, including the Xerox Retirement Income Guarantee Plan ("the Xerox Plan" or "the Plan"), do not calculate the offsets in this way. For example, the Xerox Plan calculates the offset taking into account subsequent changes in investment returns and interest rates to ensure that employees who

receive benefits before retirement are treated the same as employees who receive their benefits at retirement. The Second Circuit has held that ERISA permits the Xerox Plan to calculate the offset for prior distributions in this manner. *Frommert* v. *Conkright*, 433 F.3d 254 (2d Cir. 2006). In this case, the Ninth Circuit has held that ERISA does *not* permit the Xerox Plan to calculate the offset in this manner. As a result, a nationwide pension plan covering 40,000 employees and retirees is lawful in one circuit and unlawful in another, and the lawfulness of numerous other pension plans is called into question. Such a conflict is intolerable, and only this Court can resolve it.

1. Many pension plans coordinate the benefits they provide with benefits available to the employee from other employer-funded sources, such as the employer-funded portion of Social Security, see, *e.g.*, *Alessi* v. *Raybestos-Manhattan, Inc.*, 451 U.S. 504, 514-15 (1981), or another ERISA plan sponsored by the same or a related employer, see, *e.g.*, *Williams* v. *Caterpillar, Inc.*, 944 F.2d 658, 661-66 (9th Cir. 1991). Coordinating benefits guarantees that the employee receives a minimum level of retirement income when that income is derived from more than one source. Coordination typically is accomplished by applying an offset, so that the formula for determining the employee's accrued pension benefit includes a reduction, or "offset," for the benefit available from the other source.

When the employee has received a benefit distribution from the other source *before* retirement, the offset in the pension plan almost always takes into account the prior distribution and adjusts it to reflect its value at the time of retirement. Otherwise, employees who receive prior distributions would enjoy a benefit from the other source but not have it reflected in the offset to their pension benefit. If this were permitted, employees who receive benefit distributions before retirement would enjoy greater total benefits than employees who receive all their benefit distributions at retirement. For this reason, pension plans

commonly include offsets for prior distributions and, for some purposes, are required to do so.[1]

One common way to coordinate benefits is through a "floor-offset" arrangement. Under a floor-offset arrangement, an employee's pension benefit is coordinated with the benefit provided by a separate defined contribution account funded by the employer. A defined contribution account provides an employee with a retirement benefit based solely on the contributions and forfeitures allocated to the account and the investment returns on those amounts. ERISA § 3(34) & (23)(B), 29 U.S.C. § 1002(34) & (23)(B). Because investment returns are subject to market fluctuation, a defined contribution account cannot guarantee a minimum level of retirement income. A defined benefit pension, by contrast, can guarantee a retirement benefit that is specified by the terms of the plan. ERISA § 3(35) & (23)(A), 29 U.S.C. § 1002(35) & (23)(A). By coordinating an employee's pension benefit with the benefit provided by a defined contribution account, floor-offset arrangements offer employees the best of both worlds—the upside investment potential of a defined contribution account *and* a minimum level of retirement income guaranteed by the defined benefit pension.

In a floor-offset arrangement, the employee's accrued pension benefit is defined as the minimum benefit guaranteed under the arrangement (usually expressed as a function of the employee's pay and service) offset by the benefit provided by the employee's defined contribution account (including the benefit that would have been pro-

---

[1] See, *e.g.*, Rev. Rul. 76-259, 1976-2 C.B. 111 (App. 96a-98a) (offset for benefits provided under another ERISA plan required to include offset for prior distributions from the other plan); see also, *e.g.*, 26 C.F.R. § 1.401(a)(4)-3(f)(7) (requiring prior distributions to be taken into account in testing pension benefits for tax-qualification purposes); Prop. Treas. Reg. § 1.415(b)-2, 70 Fed. Reg. 31,213 (May 31, 2005) (same).

vided by any prior distributions from the account). Under the arrangement, an employee always receives the balance remaining in the account at retirement. If the balance, together with any prior distributions from the account, are sufficient to provide the guaranteed minimum benefit, the employee receives no benefit from the defined benefit pension side of the arrangement. If the balance and any prior distributions are not sufficient, the defined benefit pension steps in and makes up the difference.

Floor-offset arrangements use a variety of actuarial methods to calculate the benefit that would have been provided at retirement by any prior distributions from the account. Some do so by assuming the prior distribution remained in the account until retirement earning the same investment return as the accounts of other employees who wait until retirement to receive their distributions, and by then converting the accumulated balance at retirement into an actuarially equivalent pension benefit. Other arrangements skip this intermediate step and convert the prior distribution directly into an actuarially equivalent pension benefit. To determine actuarial equivalence, different floor-offset arrangements use different interest and mortality assumptions. For example, some use fixed interest and mortality assumptions, while others use variable assumptions in effect at differing times, such as when the employee's pension benefit begins, when the employee attains retirement age, or when the prior distribution occurred. The variety of methods used by floor-offset arrangements to calculate offsets for prior distributions parallels the variety of methods used for the same purpose by other plans that coordinate pension benefits with other sources of retirement income.

The IRS approved floor-offset arrangements in Revenue Ruling 76-259, 1976-2 C.B. 111 (App. 96a-98a). See *Lunn* v. *Montgomery Ward & Co.*, 166 F.3d 880, 881 (7th Cir. 1999). Because the revenue ruling applies for both tax-qualification and ERISA-compliance purposes, see *id.*, floor-offset arrangements have been structured to comply

with the ruling ever since. Under the ruling, an employee's accrued pension benefit must include an offset for the benefit provided by the employee's defined contribution account, including the benefit that would have been provided by any prior distributions from the account. While the plan must state the actuarial basis it will use to calculate the benefit that would have been provided by any such prior distributions, the ruling does not prescribe any specific method for making that calculation.

2. The Xerox Retirement Income Guarantee Plan is a floor-offset arrangement. Under the arrangement, the employee always receives the balance in his or her defined contribution account. If the balance and any prior distributions from the account fall short of providing the Plan's guaranteed minimum benefit, the employee's defined benefit pension steps in and makes up the shortfall. Consistent with Revenue Ruling 76-259, the employee's accrued pension benefit is determined by applying an offset that includes the benefit that would have been provided by any prior distributions the employee received from the account. To calculate the offset, the Plan uses the first method described above, that is, it (1) assumes that the prior distribution remained in the account until retirement earning the same investment return as the accounts of other employees who wait until retirement to receive their distributions, and then (2) converts the accumulated balance at retirement into an actuarially equivalent pension benefit. To determine actuarial equivalence, the Plan uses variable interest and mortality assumptions in effect at the time the employee's pension benefit begins.

3. Each Respondent is a current or former employee of Xerox and a current or former participant in the Plan. Each left his job at Xerox in 1983, received a distribution of his entire retirement benefit at that time, and later resumed his employment with Xerox. The distribution each Respondent received when he left Xerox in 1983 was paid from his defined contribution account. In each case, the

benefit provided by the defined contribution account exceeded the minimum retirement benefit guaranteed to the Respondent based on his pay and service at that time. As a result, none of the Respondents received any payment from the defined benefit pension side of the Xerox floor-offset arrangement.

Each Respondent was rehired by Xerox between 1987 and 1989. Upon rehire, each Respondent received credit for his prior pay and service with Xerox for purposes of calculating the minimum benefit guaranteed under the Plan. Thereafter, each Respondent's guaranteed minimum benefit grew as he accumulated additional pay and service with Xerox. When Xerox was asked to calculate the benefit to which each Respondent was entitled under the Plan in 1998, the plan administrator first calculated the Respondent's guaranteed minimum benefit based on all pay and service with Xerox – including pay and service before 1983. The plan administrator then applied an offset that included the benefit that would have been provided by the prior distribution the Respondent received from his defined contribution account in 1983. This time, the minimum retirement benefit slightly exceeded the benefit provided by each Respondent's defined contribution account (including the benefit attributable to the prior distribution). Each Respondent was informed that he would receive a benefit from the defined benefit pension side of the Xerox floor-offset arrangement, but that the benefit would be relatively small.

4. Contending that the Plan's method for calculating the offset for prior distributions short-changed them, Respondents brought this action in the United States District Court for Central District of California under 29 U.S.C. § 1132. Respondents claimed, *inter alia*, that the Plan's method of calculating the offset for prior distributions results in a forfeiture of their accrued pension benefits in violation of ERISA § 203(a), 29 U.S.C. § 1053(a); that Revenue Ruling 76-259 is inconsistent with ERISA to the extent it purports to authorize the Plan's floor-offset

arrangement; and that the Plan's disclosure of the offset had been inadequate. In a detailed opinion, the district court rejected Respondents' claims. (App. 33a-38a.)

5. The Ninth Circuit reversed, holding that the Plan's method of calculating the offset for prior distributions violates "the substantive requirements of ERISA." (App. 17a.) In the court's view, ERISA prohibits the offset for prior distributions in a floor-offset arrangement from exceeding the minimum benefit guaranteed the employee at the time of the prior distribution, even if the prior distribution would have provided the employee a larger benefit at retirement. (App. 19a-23a.) Under the court's opinion, the only way to calculate the offset for prior distributions in a floor-offset arrangement is to set the offset equal to the lesser of (1) the minimum benefit guaranteed the employee at the time of the prior distribution, or (2) the benefit the prior distribution would have provided the employee at retirement.

Petitioners sought rehearing, contending that the court's decision conflicted with its own previous decision in another case rejecting an identical challenge to the Xerox Plan, *Hammond* v. *Xerox Corp. Ret. Income Guar. Plan*, 225 F.3d 662 (9th Cir. 2000) (mem.), with this Court's decision in *Alessi*, and with decisions of other courts of appeal, and effectively invalidated all floor-offset arrangements nationwide. The court denied rehearing but issued an amended opinion.

In contrast to its original opinion, the amended opinion held that ERISA permits the offset for prior distributions in a floor-offset arrangement to equal the benefit the prior distribution would have provided the employee at retirement. (App. 8a.) However, the court still found that the Plan's method of calculating the offset violates ERISA. (App. 5a.) The court reached this conclusion because it found that ERISA requires a defined benefit pension plan to calculate an offset for a prior distribution as the "actuarial equivalent" of the prior distribution using solely in-

terest, mortality, and other assumptions in effect at the time the prior distribution was paid. (App. 8a-10a.) Any other method using any other assumptions does not yield an actuarially equivalent result and therefore violates ERISA. (*Id.*) The court found that this requirement applies to all defined benefit pension plans, whether they are part of a floor-offset arrangement or not. (App. 10a.) In the court's view, the Xerox Plan failed this requirement because it calculated the offset "based on later developments," including investment returns and other factors in effect after the prior distribution was paid. (App. 10a.)

REASONS FOR GRANTING THE WRIT

Review should be granted because the Ninth Circuit's decision directly conflicts with the decision of the Second Circuit in *Frommert* v. *Conkright*, 433 F.3d 254 (2d Cir. 2006), placing the Xerox Plan in an untenable position – lawful in one circuit, unlawful in another, frustrating Congress's goal of "uniform national treatment of pension benefits." *Patterson* v. *Shumate*, 504 U.S. 753, 765 (1992). Review should also be granted because the Ninth Circuit's decision poses a question of national importance: Offsets for prior distributions permeate the pension system, and most pension plans do not calculate the offsets in the manner prescribed by the Ninth Circuit. Thus, numerous other pension plans nationwide will be placed in the same untenable position as the Xerox Plan. Finally, review should be granted because the decision below is based on an unfounded interpretation of ERISA.

1. Review should be granted to resolve the conflict between the Ninth Circuit and the Second Circuit with respect to the lawfulness of the Xerox Plan's offset for prior distributions. That conflict places Petitioners and the sponsors of numerous other pension plans in an untenable position with regard to plan administration that only this Court can resolve.

In *Frommert*, the Second Circuit held that ERISA permits the method of determining the offset for prior

distributions that the Ninth Circuit has held ERISA prohibits. The *Frommert* plaintiffs were another group of Xerox employees who, like Respondents, left the company and later were rehired. Those plaintiffs claimed, *inter alia*, that the Xerox Plan had not properly disclosed the offset for prior distributions and that the offset caused a forfeiture in violation of ERISA § 203(a)(2), 29 U.S.C. § 1053(a)(2). The district court rejected both claims, granted summary judgment in favor of Xerox, and dismissed the action. *Frommert* v. *Conkright*, 328 F. Supp. 2d 420, 429, 432-37, 438 (W.D.N.Y. 2004). Citing *Alessi* and another district court decision rejecting essentially the same challenge to the offset, *Hammond* v. *Xerox Corp. Retirement Income Guaranty Plan*, No. CV 2:97-8349, 1999 WL 33915859 (C.D. Cal. Apr. 8, 1999), *aff'd*, 225 F.3d 662 (9th Cir. 2000) (mem.), the district court stated:

> This claim is little more than a restatement of plaintiffs' other claims, inasmuch as it, too, is premised on plaintiffs' allegation that defendants wrongfully applied the [so-called] phantom account offset when calculating plaintiffs' benefits. As explained, this did not reduce plaintiffs' accrued benefits, and no forfeiture occurred. See *Alessi* v. *Raybestos-Manhattan, Inc.*, 451 U.S. 504, 512-17 (1981) (ERISA's nonforfeiture provisions did not prohibit offset of pension benefits by workers' compensation awards; "the statutory definition of 'nonforfeitable' assures that an employee's claim to the protected benefit is legally enforceable, but it does not guarantee a particular amount or a method for calculating the benefit"); *Hammond*, [1999 WL 33915859, at *14] ("Although *Alessi* dealt with the question of whether benefits derived from sources external to the pension plan could be offset against amounts owed under the plan, its basic observations are even more compelling where previously distributed benefits under the plan itself are offset"). The purpose, and effect, of the offset is not to take away an earned

> benefit, but only to prevent a windfall to participants, which is exactly what would happen if prior distributions were ignored. *Hammond*, [*id.* at *11].

Frommert, 328 F. Supp. 2d at 438.

On appeal, the Second Circuit vacated the district court's judgments, "except as to the anti-forfeiture claim under § 203(a)(2) and an injunction under § 502(a)(3), which we affirm." 433 F.3d at 273. Although the court held that Xerox had not sufficiently disclosed the offset to pre-1998 rehires, *id.* at 266-68, and therefore could not lawfully apply the offset to those rehires, *id.* at 268, the court also held that the offset "may permissibly be applied" to employees rehired after adequate disclosure was made, *id.* at 263, 269, because "these rehired employees, unlike their predecessors who lacked such information, had the opportunity to make an informed decision about the terms of the deal offered to them under the Plan," *id.* at 269.

Thus, the Second Circuit has ruled that ERISA permits the Xerox Plan, with proper disclosure, to apply the offset for a prior distribution calculated as if that distribution had not been made until retirement – just what the Ninth Circuit held ERISA forbids. This conflict places the Xerox Plan Admininistrator, and the administrators of other pension plans that also apply offsets for prior distrbutions, in an impossible position. Under ERISA § 404(a)(1), 29 U.S.C. § 1104(a)(1), the Xerox Plan Administrator must apply the Plan's offset if the Second Circuit's ruling is correct; but the Plan Administrator may *not* apply the Plan's offset if the Ninth Circuit's ruling is correct. Only this Court can resolve the conflict.

2. Review should also be granted because the Ninth Circuit's decision has far-reaching implications for the nation's pension system. The court's decision is not limited to the calculation of benefits in floor-offset arrangements but reflects the court's view of what ERISA re-

quries of any defined benefit pension when it calculates an offset for a prior distribution. (App. 10a.) Thus, the Ninth Circuit's decision affects the calculation of accrued pension benefits under a myriad of pension offset arrangements, such as plans that apply offsets for Social Security benefits, benefits provided by another pension plan, workers' compensation payments, commissions paid after retirement, and severance benefits, along with simple offsets for prior distributions from the same plan. (See pp. 14-15, *infra*.) Indeed, a regulation recently proposed by the Treasury Department would require *all* defined benefit pension plans to calculate offsets for prior distributions in a manner that cannot be reconciled with the Ninth Circuit's ruling. (See note 3, *infra*.)

Nor is the effect of the Ninth Circuit's decision limited to the Ninth Circuit. An employer cannot create a separate plan for each federal judicial circuit; in an economy with a workforce as mobile as ours, such a system is unworkable. Even if employers could create a separate plan tailored to the law of each circuit, such a result would frustrate Congress's goal of "uniform national treatment of pension benefits," *Patterson*, 504 U.S. at 765. Either way, the Ninth Circuit's decision affects pension plans nationwide.

3. Finally, review should be granted because the Ninth Circuit's decision is wrong. First, there is no basis in ERISA or its implementing regulations for the court's holding that offsets for prior distributions may be calculated only in the manner presecribed by the court. Second, the court's holding that ERISA permits offsets to be calculated only in the manner prescribed by the court is inconsistent with the broad latitude that this Court has recognized ERISA affords plan sponsors, and on which plan sponsors have relied, to design their pension plans. Third, the Ninth Circuit's decision invalidates sound methods for calculating offsets and irrationally discriminates among employees based on when they receive retirement benefits.

a. The Ninth Circuit's construction of ERISA finds no support in the text of the statute or its implementing regulations.

ERISA § 203(a) forbids the forfeiture of accrued benefits, and ERISA § 204(c)(3) requires that, when an accrued benefit is paid in a form other than a normal retirement annuity, the payment must be actuarially equivalent to the employee's normal retirement annuity. 29 U.S.C. §§ 1053(a), 1054(c)(3). This requirement ensures that an employee is not short-changed when receiving the benefit that the employee has accrued in a form that is different than the form in which the benefit has been promised. But neither of these rules requires a plan to provide a particular level of benefits or to calculate benefits in a specific way. As the Court stated in *Alessi*, the statute "does not guarantee a particular amount or a method for calculating the benefit" that an employee may accrue. 451 U.S. at 511-12; *see also* ERISA § 3(23)(A), 29 U.S.C. § 1002(23) (App. 42a-43a) (defining "accrued benefit" in a defined benefit plan as "the individual's accrued benefit *determined under the plan*") (emphasis added).

The Ninth Circuit, however, imposed a three-step limitation on the use of offsets in determining accrued benefits: (1) In a defined benefit plan that coordinates benefits with the benefits provided from other sources, an employee's "accrued benefit" must be the minimum guaranteed benefit, as though there were no benefits paid from another source; (2) the offset for benefits from another source therefore results in a forfeiture of an employee's accrued benefit, unless the offset satisfies the actuarial equivalence rule; and (3) the actuarial equivalence rule is satisfied only if the offset is equal to the actuarial equivalent of the benefit provided by the other source, determined based on interest rates and other assumptions in effect at the time the other benefits are paid. (App. 7a-9a.)

To reach this result, the Ninth Circuit relied on a Treasury regulation, which permits a plan to apply an offset for prior distributions from the same plan, but does not specify how that offset should be calculated. (App. 7a (citing 26 C.F.R. § 1.411(a)-7(d)(6).[2]) Furthermore, the same regulation allows pension plans to value a prior distribution for a related purpose in a different way. When an employee leaves and receives a distribution of a portion of his or her benefit but is later rehired, a pension plan may condition credit for prior service on repayment of the value of the prior distribution. The regulation permits the plan to determine the value of the prior distribution using interest rates in effect at the time of the repayment, rather than the time of the prior distribution. See *id.* § 1.411(a)-7(d)(2)(ii)(B) & (d)(4)(iv)(C) (App. 85a, 91a). The Treasury Department therefore permits a method for valuing a prior distribution that the Ninth Circuit concluded would not be actuarially equivalent and thus forbidden *by the same regulation.*[3]

b. Absent a statutory limitation on the calculation of offsets for benefits from other sources, the general rule for

---

[2] 26 C.F.R. § 1.411(a)-7(d) ("Rules relating to certain distributions and cash-outs of accrued benefits") (App. 84a-95a). It is doubtful this regulation even applies to Respondents' situation. The regulation addresses the forfeiture of the portion of an employee's accrued benefit that remains in a plan when an employee terminates employment, receives less than the entire accrued benefit, and later returns to employment. *See* 26 C.F.R. § 1.411(a)-7(d)(4)(iv)(A)(1) (App. 90a). No portion of any Respondents' accrued benefit remained in the Xerox Plan after they first left Xerox.

[3] See also Prop. Treas. Reg. 1.415(b)-2(b)(1)(ii)(B)(2), 70 Fed. Reg. 31,213, 31,238 (May 31, 2005) (proposed regulation implementing limit in 26 U.S.C. § 415(b) on defined benefit plan benefit would require consideration of participant's prior defined contribution account distributions, calculated in ways inconsistent with the Ninth Circuit's decision).

determining accrued benefits under ERISA applies. In *Alessi*, the Court construed ERISA to give employers wide latitude regarding offsets in accrued benefit calculations. The Court rejected a claim by retirees that a plan's offset for workers' compensation benefits resulted in an unlawful forfeiture of an accrued benefit. The Court explained that the "accrued benefit" under the plan was an amount remaining after – not before – the offset was taken into account; the offset did not result in a forfeiture because the offset was part of the formula used to calculate the accrued benefit in the first instance. 451 U.S. at 511-12.

> [W]hat defines the content of the benefit that, once vested, cannot be forfeited? ERISA leaves this question largely to the private parties creating the plan. That the private parties, not the Government, control the level of benefits is clear from the statutory language defining nonforfeitable rights as well as from other portions of ERISA.

Id.

Thus, ERISA sets some explicit "outer bounds on permissible accrual practices," *id.* at 512 – none of which apply in this case – but otherwise affords pension plans wide latitute in defining how the accrued benefit will be calculated. Although the Ninth Circuit acknowledged that offsets are permitted by ERISA after *Alessi*, its decision straightjackets plans when it comes to calculating the offsets. Since *Alessi*, other courts of appeals have found no such limitations on offsets. See, *e.g.*, *Brengettsy* v. *LTV Steel (Republic) Hourly Pension Plan*, 241 F.3d 609, 610-12 (7th Cir. 2001) (addressing offset in floor-offset arrangement); *PPG Indus. Pension Plan A* v. *Crews*, 902 F.2d 1148, 1150-51 (4th Cir. 1990) (offset for workers' compensation benefits); *Bonovich* v. *Knights of Columbus*, 146 F.3d 57, 61-62 (2d Cir. 1998) (offset for sales agents' renewal commissions); *Vintilla* v. *U.S. Steel Corp. Plan for Employee Pension Benefits*, 606 F. Supp. 640, 642-44

(W.D. Pa. 1985) (offset for severance benefits), *aff'd mem.*, 782 F.2d 1033 (3d Cir. 1986) (table).

Discussion of one of those cases will illustrate that other courts of appeals have not imposed limits on offsets akin to the limitation imposed by the Ninth Circuit. In *Brengettsy*, the plaintiff argued that the offset for a distribution from his defined contribution account must be based upon the interest rate in effect at the time he received that distribution – a position consistent with the Ninth Circuit's rule. Citing *Alessi*, the Seventh Circuit rejected this argument, allowing the offset to be determined using interest rates in effect at another time. 241 F.3d at 610-12.

c. The Ninth Circuit's decision requires a method of calculating offsets for prior distributions that irrationally prohibits a plan from treating employees who receive benefits before retirement the same as employees who do not. When the IRS approved floor-offset arrangements in Revenue Ruling 76-259, the agency required that such plans must provide an offset for prior distributions. *See* 1976-2 C.B. 111 (App. 96a). The IRS did so to protect the integrity of the floor-offset arrangement. Otherwise, the size of an employee's benefit would vary depending on whether the employee received a distribution before retirement.[4]

---

[4] The IRS ruling also states that the floor-offset plan "must specify the time as of which such determination [of the benefit that the prior distribution would have provided at retirement] is made (the determination date) in a manner which precludes discretion on the employer." Rev. Rul. 76-259 (App. 97a). The IRS does not require the plan to determine the offset as of any particular time; it merely requires that the "determination date" be specified so that the plan sponsor may not change it after benefits have been earned. The Ninth Circuit, on the other hand, ruled that ERISA requires that what is, in effect, the "de-

Under the Xerox Plan, the offset for a prior distribution is calculated by determining the value of the benefit that the distributed funds would have provided if they had remained in the employee's defined contribution account and were invested as the other employees' accounts were invested. Consistent with the IRS's goals, this method achieves equal treatment between participants who receive prior distributions and participants whose funds remain in the Plan until retirement.

The Ninth Circuit's decision requires a different result. Under its approach, the offset is determined using different actuarial factors, depending on when the employee receives a distribution from the other source of benefits. It is impossible to know, at the time a plan is designed, whether the Ninth Circuit's method or the Xerox method will favor or disfavor employees; the outcome depends on later events. What is known, however, is that the Xerox method places employees in the same position regardless of when they receive the distribution from the defined contribuiton account. In this case, economic circumstances since 1983 have allowed securities and other investments of the defined contribution plan to outpace 1983 interest rates, so valuing the offset by the benefit the distributed funds would have provided through such investment generates a larger offset (and thus a smaller defined benefit plan benefit at retirement) than the Ninth Circuit method.[5] If, however, economic circumstances between the times of a given employee's distribution and retirement are such that later investments lag initial interest rates, the Ninth

---

termination date" must always be the date of the prior distribution.

[5] It is because the outcome of the Xerox Plan's method is known, years after the prior distribution, to create a larger offset, that the Respondents have challenged it as creating a forfeiture.

Circuit method would increase offsets and lower retirement benefits. Indeed, although the Ninth Circuit seemed to conclude that only its method would ensure actual equivalence between the prior distribution and the benefit that would result at retirement, actual equivalence would occur only in the extremely unlikely situation in which the defined contribution plan's later investments exactly matched interest rates at the time of distribution.

Under ERISA, as construed by the Second Circuit, other courts, and the IRS, Xerox's method of calculating an offset would be among the permissible methods. The Ninth Circuit's decision that *only* a different method is permitted by ERISA creates a inter-circuit conflict that stymies the uniform application of this statute and hinders the operation of nationwide pension plans such as the Xerox Plan.

CONCLUSION

The petition should be granted.

Respectfully submitted,

MICHAEL D. RYAN
XEROX CORPORATION
800 Long Ridge Road
Stamford, CT 06904

RICHARD C. SHEA
DAVID H. REMES
Counsel of Record
THOMAS L. CUBBAGE III
ROBERT S. NEWMAN
MICHAEL E. PAULHUS
COVINGTON & BURLING LLP
1201 Pennsylvania Ave., N.W.
Washington, D.C. 20004-2401
(202) 662-6000

January 2007

Attorneys for Petitioners